UNITED STATES COURTS
SOUTHERN DISTRICT OF TEXAS
FILED

DEC 2 1 2001

Michael N. Milby, Clerk

IN THE UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

MARK NEWBY, Plaintiff, v. ENRON CORPORATION, ANDREW S. FASTOW, KENNETH L. LAY, and JEFFREY K. SKILLING, Defendants.	C.A. No. H-01-3624 JURY TRIAL DEMANDED
HENRY H. STEINER, Individually and on Behalf of All Others Similarly Situated, Plaintiff, v. ENRON CORP., KENNETH L. LAY, JEFFREY K. SKILLING, ANDREW S. FASTOW, and ARTHUR ANDERSEN LLP, Defendants.	C.A. No. H-01-3717 JURY TRIAL DEMANDED

MEMORANDUM OF LAW OF HENRY H. STEINER
IN SUPPORT OF HIS OBJECTION TO CONSOLIDATION OF THE
<u>FEDERAL SECURITIES ACTIONS INVOLVING ENRON CORPORATION</u>

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INTRODUCTION

Plaintiff Henry H. Steiner, who has brought a class action on behalf of purchasers of only the preferred stock of Enron Corporation ("Enron" or the "Company"), objects to the consolidation ordered by this Court on December 12, 2001 to the extent it consolidated the claims of purchasers of Enron's various preferred shares with the federal securities fraud claims of purchasers of Enron's common stock (the "Consolidation Order"). Mr. Steiner does not oppose, and indeed, urges the coordination of all of the federal securities actions before one judge for discovery and pretrial purposes. Mr. Steiner believes, however, that consolidation of the preferred shareholders' claims with those of the common shareholders would prejudice the preferred shareholders' rights.

This objection to consolidation is being filed simultaneously with a motion to appoint separate lead plaintiffs and lead counsel for the class of Enron preferred stock purchasers. The Declaration of Steven R. Wolfe accompanies both this memorandum objecting to consolidation and the preferred purchasers lead plaintiff motion.

The Court is faced with two distinct claimant groups. The first claimant group, consisting of preferred shareholders of Enron (the "Preferred Shareholder Claimants"), is represented exclusively only in Mr. Steiner's preferred shareholder action (the "Steiner Action" or the "Preferred Shareholder Action"). The Steiner Action is brought on behalf of the following two classes: (1) a Federal Claim Class including all those who purchased the preferred stock of Enron between November 28, 1998 and November 28, 2001, inclusive; and (2) a Negligent Misrepresentation Claim Class including all those who purchased the preferred stock of Enron between January 21, 1997 and November 27, 1998, inclusive. The Steiner action alleges violations of section 10(b) of the Securities Exchange Act of 1934 ("1934 Act"), 15 U.S.C. §78j(b), and Rule 10b-5 against Enron, certain officers and directors, and Arthur Andersen LLP, Enron's independent accountant and auditor. It also alleges violations of section 20(a) of the 1934 Act, 15 U.S.C. § 78t(a) against individual defendants Kenneth Lay, Jeffrey Skilling and Andrew Fastow, as well as a negligent misrepresentation claim against all defendants. The other pending federal securities cases bring claims on behalf of, among others, purchasers of Enron's common stock (the "Common Stockholder Claimants") and allege violations of sections 10(b) and 20(a) against Enron and its officers and directors.

Given the nature of defendants' alleged fraud and the differences between Enron's common and preferred stock as investment vehicles, the fraud claims of the Preferred Shareholder Claimants are clearly distinct from those of the Common Shareholder Claimants. Those differences create conflicts between the two claimant groups with regard to presentation of proof, calculation of damages, and settlement. Additionally, there are potential Texas state law claims for negligent misrepresentation relating to prospectus liability for two Enron preferred stock IPOs, a claim not available to the common share purchasers.

The differences between the two claimant groups were emphatically reinforced when the Company filed a voluntary petition for relief under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Southern District of New York on December 2, 2001. When the claims of the two claimant groups are pressed in Bankruptcy Court, the Bankruptcy Code will provide for priority of payment for the claims of the preferred shareholder including the securities fraud claims.[1] Such disparate treatment under the Bankruptcy Code of the two Claimant groups creates a true conflict between them and disables Enron's common shareholders from properly representing the interests of the preferred shareholders in a consolidated action.[2] Further, the two Claimant groups have substantially different factual claims against non-bankrupt defendants, such as Arthur Andersen, because the investors in Enron common stock, wholly an equity instrument, and investors in Enron Preferred Stock, which partakes of debt characteristics, relied on different financial disclosures to assess the wisdom of their investments. (Wolfe Decl. ¶¶ 12-18.)

Although the actions of the Preferred Shareholder Claimants and the Common Shareholder Claimants are "related" under Local Rule 7.6, consolidation of related cases is not automatic and is dependent on the underlying facts of each case. Here, where there are substantial differences between the claimant groups in terms of the impact of the defendants' fraud upon them, the calculation of damages, and recovery potential under the federal bankruptcy laws, consolidation of all the federal securities actions is not appropriate under Rule 42(a) of the Federal Rules of Civil Procedure. Neither do these circumstances satisfy the strictures of Section 21D(a)(3)(B)(ii) of the Private Securities Litigation Reform Act ("PSLRA"), which requires that claims be "substantially the same" before consolidation "for all purposes" is appropriate. Here, the different claims and classes make coordination, not consolidation, of the preferred and common stock actions appropriate.

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[1] See 11 U.S.C.A. §§ 510(b) and 1129(b)(2)(B).

[2] Mr. Steiner believes coordination of discovery between the preferred and common stock actions would avoid any unnecessary costs or delay to the parties and would promote judicial economy.

BACKGROUND

More than 30 federal securities actions are presently pending in this district against Enron and some of its officers. All but one of those cases are brought, *inter alia*, on behalf of Enron's common stockholders. The Steiner Action on the other hand, is the only case brought exclusively on behalf of purchasers of Enron's preferred shares.

On or about June 1, 1999, Enron entered into the first of its "structured finance arrangements" with two limited partnerships that were managed by Enron's Chief Financial Officer, defendant Andrew S. Fastow.[3] Thereafter, Mr. Fastow's two limited partnerships engaged in billions of dollars of complex hedging transactions with Enron involving company assets and millions of shares of Enron stock. (¶ 84) These hedge transactions, which were in the energy and communications markets, including the broadband communications market, committed Enron to forward contracts to purchase its own shares at the market price on a given day (¶ 49), and exposed the Company to materially increased risk and uncertainty in the form of materially increased leverage and investment exposure (¶¶ 38, 39), and the failure to disclose these transactions and their impact in Enron's earning reports (of concern to common purchasers) and their impact on the balance sheet (of concern to preferred purchasers) was the proximate cause of the damages suffered by investors during the Class Period. (¶ 46.)

On October 16, 2001, Enron announced that the Company was taking a non-recurring charge of $1.01 billion after-tax for the third quarter of 2001. (¶ 71.) On October 18, 2001, Enron chairman and defendant Kenneth Lay was quoted as stating that approximately $35 million of those charges was related to transactions with Mr. Fastow's limited partnerships. (¶ 85.) Mr. Lay explained that approximately 55 million Enron shares had been repurchased by Enron as it "unwound" its participation in those transactions. Those 55 million shares had been contributed to a "structured finance vehicle" more than two years earlier in which Enron and LJM2, one of Mr. Fastow's limited partnerships, were the only investors. The transaction had aimed to provide hedges against fluctuating values of some of Enron's Broadband telecommunication and other technology

[3] *See* ¶ 46 of the Amended Class Action Complaint (the "Complaint") filed in the Steiner Action. References to the Complaint will hereinafter be designated ¶ ___.

investments, and in exchange for Enron stock, LJM2 had provided Enron with a note. The Company further disclosed on October 18, 2001, that its repurchase of the 55 million shares further reduced Enron's shareholders' equity by $1.2 billion. This reduction damaged the Company's debt to equity ratio and endangered the Company's standing with debt rating agencies. (¶ 85.)[4]

Defendants' false and misleading statements regarding the "structured finance arrangements" with Mr. Fastow's limited partnerships affected the two claimant groups differently because of the differences in their respective investment vehicles. The value of preferred stock is derived from stockholder equity, is based in part on the credit rating of the company, and generally trades much more like a corporate bond than does common stock.[5] Common stock, on the other hand, most often trades on the basis of a combination of present and expected future earnings and growth. Purchasers of preferred stock rely on the seniority of its claim on corporate assets to assure the value of their investment. (Wolfe Decl. at ¶ 12.)

Preferred Stock purchasers pay a premium for what is, in effect, a guaranteed return: they have set dividend payments and priority if the company is sold or liquidated. (Wolfe Decl. at ¶ 13.) On the other hand, preferred shareholders do not share directly in the earnings growth of the enterprise and consequently are less concerned with earnings per share or future earnings growth. Id. Their principal concern is that the dividend payment is secure and that there be sufficient assets to pay off the preferred shares on liquidation of the company. (Wolfe Decl. at ¶ 13.)

From a business and financial point of view, preferred stock resembles a debt instrument, such as a bond, and mainly trades based on interest rate fluctuations. (Wolfe Decl. at ¶ 15.)

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[4] Although disastrous to Enron, the company's arrangement with Mr. Fastow's limited partnerships proved to be very lucrative to Mr. Fastow. In addition to the $7 million in management fees for 2000, and approximately $4 million in capital increases on an investment of only $3 million, Mr. Fastow was also able to earn money for the limited partnerships by betraying his fiduciary duties to Enron and its shareholders. (¶ 86.) Thus, in September 2000, Mr. Fastow's partnership invested $30 million in "Raptor III" which involved writing put options committing LJM2 to buy Enron's stock at a set price for six months. Four months into the deal, LJM2 reportedly approached Enron to settle the investment early causing LJM2 to receive its $30 million capital invested plus $10.5 million in profit. The renegotiation was commenced and completed before a precipitous decline in Enron's stock price which could have forced LJM2 to buy Enron's stock at a loss of as much as $8 dollars per share. (¶ 87.)

[5] See the Declaration of Steven R. Wolfe in Support of proposed preferred lead plaintiffs Motion to Appoint separate Lead Plaintiffs and Lead Counsel For Purchasers of Enron Preferred Shares, and in Support of Objection to the Order of Consolidation (the "Wolfe Decl."), attached hereto, at ¶ 12.

Accordingly, unlike common stock, preferred shares do not share the full upside potential of the company nor do they reflect short term earnings fluctuations. Id.

Accordingly, the undisclosed material information regarding Mr. Fastow's limited partnerships had materially different effects on the risk profiles and values of these different classes of stock. Wolfe Decl. at ¶ 17. Thus, Enron's failure to disclose that it was taking a $1.2 billion write-down in shareholder equity, which severely diminished the value of the preferred stock, had little impact on anticipated earnings, the key to common stock valuation. Id. ¶ 18. Similarly, the Preferred Shareholder Claimants were more greatly injured by the defendants' failure to disclose that Enron's investment and hedging deals with Mr. Fastow's limited partnerships involved forward commitments to deliver Enron stock. Those forward commitments ensured that Enron would not have to report earnings' losses on those deals, but instead could reduce shareholder equity and the liquidation value of the Company without affecting its income and earnings statements. (¶ 110(a); Wolfe Decl. at ¶¶ 18-20.)

By keeping billions of dollars of debt and trading losses off Enron's balance sheet through its complicated financing strategies with Mr. Fastow's limited partnerships, defendants left Enron liable to pay in cash or in stock if and when Enron's portfolio was marked down. (¶ 110(b)). The Preferred Shareholder Claimants suffered greater harm than did the Common Shareholder Claimants from defendant's failure to disclose the potential enormous write-downs in shareholder equity that Enron faced as a result of its structured finance arrangements with Mr. Fastow's limited partnerships. (¶ 110(d)). By putting the Company in the undisclosed position of having to repurchase 55 million shares in order to unwind a hedging transaction with Mr. Fastow's limited partnership, defendants materially increased the risk of impairing Enron's equity on its balance sheet. (¶ 110(j)). That increased risk more greatly affected the Preferred Shareholder Claimants than the Common Shareholder Stock Claimants due to the enormous reduction of shareholders' equity. (Wolfe Decl. at ¶¶ 18-20.)

Defendants further jeopardized the value of Enron's preferred shares by failing to disclose that the Company might be forced to borrow billions of dollars on its bank lines of credit, which would create debt with rights senior to that of the preferred shares. (¶ 110(e)). Defendants' undisclosed investment and hedging activities incurred a material risk of substantial deterioration of the Company's financial condition, making the preferred stock dividends less secure. (¶ 110(f)); (Wolfe Decl. at ¶23.). As Enron's preferred stock dividends were to be paid in full before any dividends were paid on its common stock, this affected the preferred shareholders more immediately. Id. Subsequent to the filing of the Steiner Action, Enron established another $1 billion - plus bank line of credit, which in the usual course would be debt senior to the preferred shares. Id.

The trading in Enron's common and preferred stock as the market learned of Enron's fraud illustrates the manner in which those stocks were affected differently by it. (See Trading Chart attached as Exhibit A to the Wolfe Decl.) As discussed below, those trading differences impact each claimant group's proof of liability and damages. (Wolfe Decl. at ¶ 25.)

The first major announcement by the Company, on October 16, 2001, of a $1.01 billion after-tax charge to earnings caused Enron common stock to decline nearly 50% over the next five trading days, while Enron's 8 1/8 R Series Preferred Shares (the "Preferred R Shares") declined only about 8% during that period. (Wolfe Decl. at ¶ 29.) This difference reflects the respective concerns of the two classes of shareholders: the common shareholders anticipated reduced earnings from the after-tax charge while the preferred shareholders did not believe the after-tax charge was large enough to affect their expected dividend payments. (Wolfe Decl. at ¶ 30.)

On November 9th, Enron announced that it had agreed to be acquired by its rival, Dynegy Inc. (Compl. ¶ 103.) The Dynegy acquisition was perceived by the market as being much more beneficial to the preferred shareholders than the common, as it promised to "better" Enron's credit and increase stockholder equity to support the dividend payments and claims of the preferred shareholders. (Wolfe Decl. at ¶ 31.) The Dynegy acquisition promised to do less for future earnings and growth, the determinants of the common stock price. Id. Accordingly, the Preferred R Shares increased in value by about 25% after the announcement while the common stock increased only 15%. Id.

Enron's preferred stock was more greatly affected than its common stock, however, when Standard and Poor's lowered Enron's credit rating to triple-B- minus on November 12, 2001. (¶ 105) Whereas the Preferred R Shares lost 8.5% of its value over the two days following that announcement, Enron's common stock gained 8% over the same time period. (Wolfe Decl., Ex. 1; ¶ 33.)

The most dramatic, and dispositive difference in the trading between the common and preferred shares concerns when each essentially lost its value (Wolfe Decl. ¶ 24.) While as of November 21, 2001, Enron common stock had lost at least approximately 90% of its value since October 16th, the price of the Preferred R Shares at that date was only approximately 44% lower than its year high on October 17th. (Wolfe Decl., Ex. 1.)

When, on November 28th , Dynegy announced it was calling off the acquisition (¶ 106), the Preferred R Shares were devastated, declining in value that day by about 90%. The likelihood that Enron would be able to pay its dividend had become extremely dubious. Enron common stock declined only $3.00 that day, the prospects for future earnings and growth already having become remote. (Wolfe Decl., Ex. A, ¶ 32)

Subsequent to the filing of the Steiner Action, Enron, on December 2, 2001, filed a voluntary petition for relief under Chapter 11 of Title 11 of the United States Code (the "Bankruptcy Code") in the United States Bankruptcy Court for the Southern District of New York. (Wolfe Decl. ¶ 11.)

Apparently the company was stealing from the preferred shareholders to bolster the price of the common stock. In the markets for forwards and derivatives, where Enron was a major player, credit-worthiness is essential. Enron's trading portfolios consisted largely of over-the-counter, private party deals. The willingness of the counter-parties to Enron's trades to accept Enron's credit was essential to Enron's viability. (Wolfe Decl. ¶ 37.)

As Enron's portfolios became ever larger and more leveraged and its misstated mark-to-markets, therefore, more onerous, the necessity to maintain the fiction that future earnings and growth were robust became more desperate. In order to support a larger and larger house of cards, Enron buried losing trades and portfolios in related, off-book entities, like LJM2, and made concealed agreements to repurchase its treasury stock with those entities. The effect of these portfolio and stock manipulations was to surreptitiously take value from shareholder equity and assets in order to support earnings, i.e., to favor common over preferred in the short-run. The preferred stock, thus, was differently inflated than the common stock throughout the class period, until the last few days (when all stock became essentially worthless.) The claims should be pursued separately, not together, in recognition of how the Enron scheme affected the two stock classes. (Wolfe Decl. ¶ 38.)

Negligent Misrepresentation Claim

A further distinction between the two claimant groups is the preferred shareholders' state law claim for negligent misrepresentation based on Enron's November 8, 2001, announcement that it was restating its earnings back to January 1, 1997. (Compl. ¶ 101.) The Steiner Action alleges a negligent misrepresentation claim, under Texas state law, with respect to the IPO trading in two classes of Enron preferred stock, based upon possible material misstatements or omissions concerning 1997 in the respective prospectuses. (Compl. ¶¶ 156-163.) As there was no common stock IPO during this period, this claim is not available to the Common Shareholder Claimants.

ARGUMENT

I. CONSOLIDATION OF THE PREFERRED SHAREHOLDERS' CLAIMS WITH THOSE OF THE COMMON SHAREHOLDERS IS NOT APPROPRIATE UNDER RULE 42 OR THE PSLRA

a. Standards for Consolidation

Rule 42 of the Federal Rules of Civil Procedure provides that the Court may order consolidation "[w]hen actions involving a common question of law or fact are pending before the court." Fed. R. Civ. P. 42(a).

Consolidation under Rule 42(a) is entrusted to the Court's sound discretion, but that discretion is subject to the Court's consideration of specific factors. In particular, the Court should weigh:

> Whether the specific risks of prejudice and possible confusion [are] overborne by the risk of inconsistent adjudications of common factual and legal issues, the burden on parties, witnesses and available judicial resources posed by multiple lawsuits, the length of time required to conclude multiple suits as against a single one, and the relative expense to all concerned of the single-trial, multiple-trial alternatives.... Care must be taken that consolidation does not result in unavoidable prejudice or unfair advantage. Conservation of judicial resources is a laudable goal. However, if the savings to the judicial system are slight, the risk of prejudice to a party must be viewed with even greater scrutiny.

Cantrell v. GAF Corp., 999 F.2d 1007, 1011 (6th Cir. 1993) (quoting Johnson v. Celotex Corp., 899 F.2d 1281, 1285 (2d Cir. 1990), cert. denied, 498 U.S. 920 (1990.) Application of these criteria here shows that consolidation of the preferred shareholders' claims with those of the common shareholders is not appropriate.

The PSLRA also provides, among other things, for consolidation of substantially similar actions. Importantly, section 21D(a)(3)(B)(ii) of the PSLRA -- which provides for the consolidation of actions "asserting substantially the same claim or claims" -- (emphasis added), creates a new and higher standard for consolidation of cases than is generally required for consolidation under Rule 42(a) of the Federal Rules of Civil Procedure. Accordingly, the circumstances presented here similarly fail to satisfy the PSLRA's more stringent strictures for consolidation.

b. The Consolidation Order Prejudices The Rights Of The Preferred Shareholders

The Fifth Circuit has emphasized that consolidation is inappropriate where, as here, obvious prejudice to the Preferred Shareholder Claimants will result from the order:

> In resorting to the use of Rule 42(a) the trial judge must be most cautious not to abuse his judicial discretion and to make sure that the rights of the parties are not prejudiced by the order of consolidation under the facts and circumstances of the particular case. Where prejudice to rights of the parties obviously results from the order of consolidation, the action of the trial judge has been held reversible error.

Dupont v. Southern Pacific Co., 366 F.2d 193, 195-96 (5th Cir. 1966); see also St. Bernard General Hospital, Inc. v. Hospital Service Ass'n., 712 F.2d 978, 989 (5th Cir. 1983) ("Consolidation is improper if it would prejudice the rights of the parties.").

Accordingly, courts will look closely at whether consolidation of cases and complaints will harm potential claims and work prejudice to a party that could be avoided absent consolidation. See Malcolm v. National Gypsum Co., 995 F.2d 346, 350 (2d Cir. 1993) (court emphasized fairness over efficiency in reversing order consolidating 600 asbestosis cases); In re Consolidated Parlodel Litig., 182 F.R.D. 441, 447 (D.N.J. 1998) (court applied Second Circuit Celotex balancing test in declining to consolidate 14 products liability actions, finding that interests of judicial economy were outweighed by concern for fair and impartial trial.

When claims particular to a party are substantially different from the other consolidated claims, and management of the consolidated cases is vested in lead counsel whose efforts are likely to focus on the interests of the majority, the minority may be prejudiced and denied full discovery and preparation. See Garber v. Randell, 477 F.2d 711, 714-716 (2d Cir. 1973) (only one of 15 plaintiffs brought cause of action against law firm, which claim was found to be too distinctive to consolidate.) Accordingly, in Robert Mark v. Fleming Companies, et al., Case No. Civ. 96-506-M (W.D. Okla. Mar. 26, 1997) (annexed hereto as Exhibit B), appeal dismissed, 146 F.3d 1224 (10th Cir. 1997), under circumstances similar to those here, the court refused to consolidate for all purposes an action filed by a group of note holders with Securities Act claims with actions filed by common shareholders alleging claims pursuant to the 1934 Act. The court also appointed separate lead plaintiffs and separate lead counsel to represent the respective claims of the common stockholders and the noteholders.

The District Court stated:

> Having carefully reviewed the parties' briefs and evidentiary materials submitted therewith, the Court finds plaintiff's arguments against consolidation persuasive. Although all ten cases are based upon the same factual underpinnings, the Court finds the claims asserted on behalf of the note holders are not substantially the same as the claims asserted by the stockholders. Therefore this case should not be consolidated with the other nine Fleming cases for trial.

Mark, slip op. at 3, 4 (Ex. B.)[6]

The Consolidation Order, by consolidating the actions of the two claimant groups, prejudices the rights of the Preferred Shareholder Claimants. As discussed above, the Preferred Shareholder Claimants suffered a distinct and greater injury than did the Common Shareholder Claimants by the defendants' fraud. The differences between the claims of the two shareholder groups is underscored by the disparate trading histories of the two classes of stock as the Company's fraud began to be understood by the market.

The Consolidation Order further threatens to leave the claims of the preferred shareholders unprosecuted, as the Common Shareholder Claimants who are considerably more numerous than the Preferred Shareholder Claimants, will seek to prove different facts than the Preferred Shareholder

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[6] In Mark, the court consolidated the cases for pre-trial purposes. Mark, slip. op. at 3-4. (Ex. B) Here, Mr. Steiner proposes coordination not consolidation at the pre-trial stage.

Claimants in order to establish liability and damages. For example, while the Preferred Shareholder Claimants will need to focus on Enron's assets, the Common Shareholder Claimants will have no interest in proving that Enron's asset base was eroding. The two claimants groups will also have materially different interests with respect to proving defendant Arthur Andersen's involvement in knowing fraud or recklessness, as each group will focus on the misstatements material to the information it relied on in making its respective investments. (Wolfe Decl. ¶ 40.)

There will also be conflicts in terms of the two claimants groups' proof of damages due to the fact that the common and preferred stock reacted differently to the curative disclosures. For example, by November 21, 2001, Enron's common stock had lost approximately 90% of its value since October 16th, while Enron's Preferred R Shares had lost only 48% of its value from that date. Hence, as the price of the Preferred R Shares did not collapse until after the November 28th announcement that the Dynegy deal had fallen through, the Preferred Shareholder Claimants will require damages to be calculated as of a later date than the Common Shareholder Claimants in order to fairly and accurately reflect their damages. (Id. at ¶ 48.) (Wolfe Decl. Ex. A.)

Finally, another crucial reason supporting the conclusion that the Steiner Action should not be consolidated with the other actions concerns conflicts with respect to any potential settlement. The allocation of any settlement normally looks at different groups or subclasses which bought similar shares, usually meaning all common shares, during a certain period of time, but such allocations usually result in an apples to apples allocation because all purchasers bought the same types of shares (usually common). Such an allocation would not work where both common and preferred stock purchasers are present, for a number of reasons.

For example, the different risk/reward ratios and risk profiles for common and preferred stock, which purchasers have in mind when they make their purchases (Wolfe Decl. ¶¶ 12-13), in themselves demonstrate that the purchasers of common and preferred shares should have separate lead plaintiffs, separate lead counsel, and that the Steiner action should not be consolidated with the other actions. This is so because common share purchasers knowingly take a much greater risk, with a much greater potential upside, than preferred stock purchasers.

Since the guiding light of the distribution of any settlement fund ultimately is true fairness, we submit that to treat the Enron common and preferred share purchasers the same and award them the same percentage recovery would be unfair. The preferred stock purchasers had an expectation of lesser risk than the risk assumed by common stock purchasers. Since the common and preferred shares are now each worth essentially zero, treating the common and preferred purchasers the same does not take into account their reasonable, different expectations. It is not equitable to require the preferred shareholders to retroactively assume a greater risk than that for which they bargained. Conversely, it is not equitable for the common share purchasers to benefit in comparison to preferred share purchasers by permitting them to assume a level of risk equal to that assumed for – not by – the preferred purchasers. See In re Cendant Corp. Litig., 182 F.R.D. 144, 149 (D.N.J. 1998) (court appointed separate lead counsel for the PRIDES purchasers, which purchasers subsequently were paid 100% of their loss in damages while all others recovered only 30% of their damages).

c. The Consolidation Order Prejudices The Preferred Shareholder Claimants' Priority Rights in Bankruptcy Court

The Consolidation Order also prejudices the Preferred Shareholder Claimants should the consolidated claims be pressed in an adversary proceeding in the United States Bankruptcy Court for the Southern District of New York. Together, sections 510(b) and 1129(b)(2)(B) of the Bankruptcy Code mandate that the preferred shareholders' claims including securities fraud claims be fully paid before the common shareholders receive any payment for their fraud claims. Under section 510(b) "damages arising from the purchase or sale of [the security of the debtor] . . . shall be subordinated to all claims or interests that are senior to or equal the claim or interest represented by such security." The prospectus for each tranche of preferred stock offered by Enron, as well as Enron's Charter, provided that the purchasers of those preferred shares had interests senior to Enron's common shareholders in terms of both dividends and liquidation.[7] Accordingly, the

[7] See Enron Capital Trust I 8:30% Trust Originated Preferred Securities Prospectus, dated 11/18/96, at p. 4; Enron Capital Trust II Prospectus, dated 1/13/97 at p. 4; Enron Capital LLC 8% Cumulative Guaranteed Monthly Inc. Pref. Shares Prospectus, dated 11/8/93 at p. 8 (no dividends to lower ranking securities until preferred shares get dividends); and p. 9 (Liquidation Distribution); Portland General Electric Company 7.75% Series Cumulative Preferred Stock Prospectus Suppl, dated 6/3/92

Preferred Shareholder Claimants will recover for their fraud claims before the Common Shareholder Claimants. And, pursuant to section 1129(b)(2)(B)[8] the Common Shareholder Claimants will recover nothing on their fraud claims until the Preferred Shareholder Claimants are fully compensated for their fraud claims.

Thus, the different recovery prospects in bankruptcy court for the two groups of class claimants further militates against consolidation. If the Consolidation Order stands, the superior rights of the Preferred Shareholder Claimants under the Bankruptcy Code will be jeopardized to the extent those rights are represented by the Common Shareholder Claimants.

d. Consolidation Would Create Juror Confusion

The mere existence of common issues does not require consolidation, especially when those common issues themselves may cause juror confusion. See Seguro de Servicio de Salud v. McAuto Systems Group, Inc., 878 F.2d 5 (1st Cir. 1989) (consolidation of two separate arbitration proceedings was abuse of discretion, as contracts requiring arbitration were governed by law of different states and contracted arbitration clauses were upon examination sharply different.) Here, where the factual underpinnings of the alleged fraud are the same with respect to the two claimant groups but the impact of those facts upon each group differs markedly, juror confusion is all but inevitable.

In In re Brand Name Prescription Drugs Antitrust Litigation, No. 94 C 897, MDL 997, 1995 WL 399684, at *2 (N.D. Ill. July 7, 1995), the District Court denied plaintiffs' motion to consolidate all conspiracy claims under the Sherman Act because, although the actions shared common questions

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at p. 6 - Under Dividend Rights, and p. 7 (Liquidation Rights); Enron Capital Resources LP Prospectus, dated 7/28/94.

8 11 U.S.C.A. § 1129(b)(2)(B) states:

(B) With respect to a class of unsecured claims --

(i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or

(ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property.

and evidence and consolidation may have served to conserve resources, jury confusion "[wa]s apt to be compounded, rather than minimized" due to the different claims made resulting in prejudice to the parties. Brand Name Prescription Drugs, 1995 WL 399684 at *2. The court concluded that "a party's individual rights must 'not be lost in the shadow of a towering mass litigation.'" Id. quoting In re Brooklyn Navy Yard Asbestos Litig., 971 F.2d 831, 853 (2nd Cir. 1992). See also Fleishman v. Prudential-Bache Sec., 103 F.R.D. 623 (E.D. Wis. 1984) (motion to consolidate five actions alleging violations of federal securities laws and state common law denied where factual dissimilarities existed and where there was a strong possibility of confusing the jury).[9]

Accordingly, the Consolidation Order should be vacated as to the Preferred Shareholder Claimants to avoid juror confusion.

II. THE PSLRA REQUIRES THAT THE QUESTION OF CONSOLIDATION BE DECIDED PRIOR TO THE DETERMINATION OF THE APPOINTMENT OF LEAD PLAINTIFF

The PSLRA states in pertinent part:

> If more than one action on behalf of a class asserting substantially the same claim or claims arising under this title has been filed, and any party has sought to consolidate those actions for pretrial purposes or for trial, the court shall not make the determination [of appointment of lead plaintiff under §21D(a)(3)(B)] until after the decision on the motion to consolidate is rendered. . . .

15 U.S.C. §78u-4(a)(3)(B)(ii).

The PSLRA thus establishes a two-step process for resolving lead plaintiff and consolidation issues where more than one action on behalf of a class asserting substantially the same claims has been filed. The court "shall" first decide the consolidation issue and thereafter decide the lead plaintiff issue, "[a]s soon as practicable" after the consolidation motion has been decided. Id.

[9] See also Schneck v. IBM Corp., Civ. No. 92-4370 (GEB), 1996 U.S. Dist. LEXIS 10126 (D.N.J. June 21, 1996) (consolidation not warranted where plaintiff sought to consolidate ten keyboard products liability cases because, while common questions of law and fact were involved, each plaintiff had individual injuries stemming from different circumstances and use patterns; that all plaintiffs were data entry clerks or typists was not enough to justify consolidation); United-States-EPA v. Green Forest, 921 F.2d 1394 (8th Cir. 1990) (district court properly denied citizens' request to consolidate Clean Water Act action with EPA's action where citizens' request for punitive damages, compensatory damages for personal injuries, and relief for many common law tort claims were not relevant to the EPA action and where the citizens' claims were to be tried before a jury, while the EPA action was to be tried before the court).

CONCLUSION

In conclusion, although Mr. Steiner recognizes that there will be some factual overlap in the cases, he does not believe that the Steiner Action should be swallowed up into another action led by plaintiffs who have true conflicts. For the reasons stated above, Mr. Steiner respectfully requests that the Consolidation Order be vacated, and that the Steiner Action not be consolidated with the pending common stock actions, but instead be coordinated with the common stock actions for discovery and pretrial purposes as may be appropriate.

Dated: December 21, 2001

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Certificate of Service

I, Robert B. Weintraub, hereby certify under the penalty of perjury that I caused to be served: (1) the Proposed Preferred Purchaser Lead Plaintiffs' motion to appoint preferred purchaser lead plaintiffs and lead and local counsel, with a Memorandum of Law, the Declaration of Jack E. McGehee with exhibits, the Declaration of Steven R. Wolfe with exhibit, and Proposed Order; and also (2) Plaintiff Henry Steiner's Objection and Memorandum of Law Opposing Consolidation with the Steven R. Wolfe Declaration, by first class mail, postage pre-paid upon the following law firms listed below.

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